By Gregory M. Gotwald[1]

Third-Party Releases: An Insurance-Coverage Perspective on the Impact of Their Loss

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As of press time, bankruptcy practitioners (and many others) are eagerly awaiting the U.S. Supreme Court's decision in *Harrington v. Purdue Pharma* and whether nonconsensual, third-party releases will be permitted under the Bankruptcy Code. This has been described as the "'great unsettled' question of bankruptcy law."[2] Practitioners and scholars with expertise ranging from bankruptcy to mass torts have opined on the merits (good and bad) of utilizing bankruptcy and nonconsensual, third-party releases to resolve mass tort liability.[3] What more can be said?

Notwithstanding, this article has some thoughts on the ramifications of utilizing bankruptcy to resolve mass torts *without* the ability to employ nonconsensual, third-party releases. The hypothesis: Parties' willingness and bankruptcy courts' ability to resolve mass torts in bankruptcy will be greatly diminished without nonconsensual, third-party releases. The reason? Insurance.

Bankruptcy Is an Effective and Efficient Tool to Resolve Mass Torts

There are inherent problems with handling mass torts outside of bankruptcy.[4] The tortfeasor lacks sufficient funds to compensate all victims, so individuals race to the courthouse to collect without regard for other victims.[5] Multi-district litigation (MDLs) and class actions move slowly.[6] Class actions have limited utility in latent personal-injury claims,[7] and MDLs suffer from their own varied flaws.[8]

While it has its critics, bankruptcy provides a more equitable and efficient resolution of mass torts. Without nonconsensual, third-party releases, *insurance* will diminish bankruptcy's efficacy in resolving mass torts. Some may view that as a positive. Why let wrongdoers off so easily?[9] For others, the realities of mass tort litigation take over. For example, there is a race to judgment among plaintiffs, assuming that they can even afford to fund the case to judgment. As courts and commentators have recognized, bankruptcy is a great — the best, even — tool for fairly and efficiently resolving mass torts:

> Chapter 11 "offers a structured system to manage multiple liabilities and has provided a forum for companies with massive liabilities to attempt to do so." Courts in bankruptcy proceedings may employ procedural mechanisms similar to those employed by nonbankruptcy courts to resolve common issues underlying multiple claims. One of the major advantages of such proceedings is that threshold issues that may be dispositive of whole categories of claims can be addressed in a uniform fashion in a single forum. Such centralized resolution of claims is difficult to achieve in the civil litigation system and has significant benefits for the consistent and efficient disposition of claims.[10]

Hon. **Robyn L. Moberly** went further in the USA Gymnastics/Larry Nassar mass tort bankruptcy:

> "[T]he principal function of bankruptcy law is to determine and implement in a single collective proceeding the entitlements of all concerned." [*Matter of American Reserve Corp.*, 840 F.2d 487, 489 (7th Cir. 1988).] The bankruptcy process has systemic advantages in that (1) claimants can file claims at little or no cost, without need of counsel; (2) properly filed claims are deemed allowed under § 502(a) if not objected to,

1 Disclosure: The author is not a bankruptcy attorney. He is an insurance-coverage attorney who assists in mass tort bankruptcies. That is the lens from which the author approaches this issue.

2 David R. Kuney, "Commentary: Reflections and Predictions on the Oral Argument in *Purdue Pharma*: The Supreme Court Should Reverse the Second Circuit," *ABI Bankruptcy Brief* (Jan. 4, 2024), at 1 (quoting *In re Purdue Pharma LP*, 635 B.R. 26, 37 (S.D.N.Y. 2021)). Prof. Kuney and a host of other ABI members with views on both sides of the case are working on a special publication to be released shortly after the Supreme Court's decision in *Purdue Pharma*. Check store.abi.org soon after the decision for its availability.

3 *Id.*; Douglas G. Smith, "Resolution of Mass Tort Claims in the Bankruptcy System," 41 *U.C. Davis L. Rev.* 1613, 1634 (2008).

4 Anthony J. Casey & Joshua C. Macey, "In Defense of Chapter 11 for Mass Torts," 90-3 *U. Chicago L. Rev.* 974, at 996-97, 980-81, 994-1001 (2023); C. Anne Malik, "Unlocking the Code: The Value of Bankruptcy to Resolve Mass Torts," U.S. Chamber of Commerce Inst. for Legal Reform, at 6-10 (Dec. 7, 2022), *available at* instituteforlegalreform.com/research/unlocking-the-code-the-value-of-bankruptcy-to-resolve-mass-torts (unless otherwise specified, all links in this article were last visited on Feb. 1, 2024).

5 Casey & Macey, *supra* n.4 at 976, 987, 994-96, 999.

6 Malik, *supra* n.4 at 6.

7 *Id.* at 8.

8 Casey & Macey, *supra* n.4 at 980-81; *see also* Malik, *supra* n.4 at 8.

9 *See, e.g.*, Kuney, *supra* n.2 at 7; "Durbin Highlights Johnson & Johnson's Shameful 'Texas Two-Step' Maneuver on Senate Floor," Press Release from the Office of Sen. Dick Durbin (Feb. 15, 2022), *available at* durbin.senate.gov/newsroom/press-releases/durbin-highlights-johnson-and-johnsons-shameful-texas-two-step-maneuver-on-senate-floor.

10 Smith, *supra* n.3 at 1634. *See also* S. Elizabeth Gibson, "Case Studies of Mass Tort Limited Fund Class Actions and Bankruptcy Reorganizations," Fed. Jud. Ctr. (2000) at 18-27, *available at* uscourts.gov/file/17903/download.

thus avoiding discovery costs; (3) it provides established mechanisms for notice and the management of large claims; (4) proceedings are centralized in a single court with nationwide service of process; and (5) all of the debtor's assets are under the control of the bankruptcy court, thus providing protection against a race to judgment by creditors. *Gentry v. Siegel*, 668 F.3d 83, 92-93 (4th Cir. 2012); *In re Bally Total Fitness of Greater New York*, 411 B.R. 142, 145-146 (S.D.N.Y. 2009).[11]

In short, there is little dispute that bankruptcy provides an efficient tool to ascertain, assess and resolve mass tort liabilities. This defense strategy's efficacy is proven by its increased commonality.[12]

Ultimately, that practical efficiency means more money to resolve the claims. Instead of paying huge amounts to defend hundreds or thousands of claims, more of that money is put toward compensation.[13]

Insurance Is a Critical Part of Resolving Mass Tort Bankruptcies

More money to resolve the claims in a mass tort bankruptcy is important, but when it comes from insurers, it can be critical to a fair, reasonably prompt resolution of claims and a successful reorganization.[14] The defendant generally lacks the funds to resolve claims; after all, it is in bankruptcy.[15] Fortunately, the bankruptcy petition does not revoke insurance,[16] making it a vital asset.

The most prevalent example has been in asbestos litigation. In 2009, the Insurance Information Institute estimated that insurers had contributed approximately $65 billion toward asbestos liabilities.[17] In the USA Gymnastics/Nassar mass tort bankruptcy, insurance funded nearly $340 million of the $380 million settlement.[18] Insurance was also critical to Boy Scouts of America's reorganization plan.[19] Similarly, insurance continues to be a key player in multiple church-related, sexual-abuse bankruptcies around the nation.[20] In short, without insurance, the funds available to compensate tort victims would be dramatically less.

The Debtor's Insurance Policies Often Cover Additional Tortfeasors

Virtually all liability policies cover more than just the named insured. If the policyholder is a company, the general liability policy routinely also insures the executive officers, directors, employees, volunteers and stockholders.[21] Directors' and officers' liability policies also typically cover the company and the individual directors and officers.[22]

As such, policyholders often connect "additional insureds" to their policies, commonly due to contractual requirements. Adding additional insureds is so prevalent that there are more than 100 standardized forms used to add additional insureds to general liability policies.[23] One of these forms automatically adds entities as additional insureds when a contract requires it.[24] It requires no additional notice to the insurance carrier.

The result is this: The debtor's policies regularly cover a variety of entities/individuals beyond the debtor. However, a problem arises when these other insureds also have liability for the torts at issue.

With mass torts, the liability exposure often abounds. With asbestos, the manufacturers, suppliers, distributors and more all have exposure. With the Boy Scouts, the regional councils also have significant exposure. In *USA Gymnastics*, the U.S. Olympic and Paralympic Committee had exposure and was insured under most of USA Gymnastics' policies. Of course, there are also the Sacklers with Purdue Pharma.

"Finality" Maximizes Settlement Funds from Insurers

There is another key benefit (beyond those listed in the "Bankruptcy Is an Effective and Efficient Tool to Resolve Mass Torts" section of this article) to resolving mass torts in bankruptcy: complete finality — that is, certainty (or as close as possible) that the claims are resolved. There are no class members who opted out, no future cases to defend[25] and no existential risk for a nuclear verdict. Any public relations nightmare associated with tort liability and/or bankruptcy generally ends.

Those who work with (or against) insurers will tell you this: Insurers pay a "premium" for finality. The debtor/policyholder often pushes insurers to resolve the claims so that it can successfully emerge from bankruptcy. The debtor may threaten the insurer with bad faith for failing to settle the claims. On top of this, insurers want to close claims and remove any remaining reserves from the books. All of this leads to insurers willing to pay more for finality, and this extra money increases the likelihood of settlement and a discharge.

Bankruptcy provides that finality with respect to the debtor better than any other option, but without nonconsensual, third-party releases, finality will be lost in many circumstances. Other insureds likely also have exposure for the underly-

11 *In re USA Gymnastics*, No. 18-09108-RLM-11, 2020 Bankr. LEXIS 1090, at *11 (Bankr. S.D. Ind. April 20, 2020). *See also In re Wildwood Vill. LLC*, No. 3:20-bk-02569-RCT, 2021 Bankr. LEXIS 1188, at *9-10, n.35 (Bankr. M.D. Fla. May 4, 2021).

12 *See, e.g.*, Miranda H. Turner, "Developments in Mass Tort Bankruptcies," 54 *The Brief* 3 at 26 (Spring 2023).

13 *See* Malik, *supra* n.4 at 7.

14 Richard Epling, *et al.*, "Intersections of Bankruptcy Law and Insurance Coverage Litigation," L. 21 *J. Bankr. L. & Prac.* 2 Art. 1.

15 *But see, e.g., In re Aearo Techs. LLC*, Nos. 22-02890-JJG-11, 22-02891-JJG-11, 22-02892-JJG-11, 22-02893-JJG-11, 22-02894-JJG-11, 22-02895-JJG-11, 22-02896-JJG-11, 2023 Bankr. LEXIS 1519, at *41-57 (Bankr. S.D. Ind. June 9, 2023).

16 State law generally requires liability policies to apply regardless of whether the policyholder is going through bankruptcy. *See, e.g.*, 215 Ill. Comp. Stat. Ann. 5/388; Md. Code Ann., Ins. § 19-102. Standard-form liability policies reflect this as well. *See, e.g.*, ISO Form CG 00 02 04 13 § IV(1).

17 "Asbestos Liability," Ins. Info. Inst. (July 9, 2009), *available at* iii.org/article/asbestos-liability. According to one law firm, there have been more than 140 asbestos-related bankruptcy filings. "Chart 1: Company Name and Year of Bankruptcy Filing (Chronologically)," Crowell & Moring LLP (revised rev. Oct. 5, 2023), *available at* crowell.com/a/web/hmiqRBhH8F99xjVHNoBcG2/20231006-list-of-asbestos-bankruptcy-cases-chronological-order.pdf.

18 *In re USA Gymnastics*, No. 18-09108-RLM-11, Findings of Fact, Conclusions of Law, and Order Confirming the Modified Third Amended Joint Chapter 11 Plan of Reorganization Proposed by USA Gymnastics and the Additional Tort Claimants Committee of Sexual Abuse Survivors, Doc. No. 1776 at pp. 68, 73-74 of 224 (Dec. 16, 2021).

19 Chad Hemenway, "Boy Scouts of America Bankruptcy Plan Upheld Despite Insurers' Objections," *Ins. J.* (March 28, 2023), *available at* insurancejournal.com/news/national/2023/03/28/714088.htm.

20 *See, e.g.*, Dietrich Knauth, "Rochester Diocese Receives Insurer's Competing $201 Million Bankruptcy Plan," *Reuters* (Sept. 5, 2023), *available at* reuters.com/legal/litigation/rochester-diocese-receives-insurers-competing-201-mln-bankruptcy-plan-2023-09-01/; Yun Park, "Insurers Blast Camden Diocese New Ch. 11 Plan," *Law360* (Nov. 9, 2023), *available at* law360.com/articles/1765048 (subscription required to view article).

21 ISO Form CG 00 02 04 13 § II.

22 *See* Epling, *supra* n.14; "Directors and Officers Insurance," Ins. Info. Inst., *available at* iii.org/article/directors-and-officers-insurance.

23 *See, e.g.*, ISO Form CG 20 02 11 85 to ISO Form CG 34 09 12 19.

24 ISO Form CG 20 43 12 19.

25 Presumably, there is a fixed amount set aside for future claims to cover them.

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ing issues. Without the nonconsensual, third-party releases, those additional insureds are not released, and true finality for the insurers is lost.

That is not to say that bankruptcy courts would be devoid of mass tort-related filings, but the "premium" that insurers pay for finality would be gone. Amounts available for settlement would be lower, which means fewer settlements. With a key objective of a mass tort bankruptcy — final global settlement — diminished, the utilization of bankruptcy to achieve that objective also would diminish.

Insurers May Be Precluded from Adequately Contributing to Settlements if Nonconsensual, Third-Party Releases Are Prohibited

The benefit of the nonconsensual, third-party release is not just increased amounts paid for finality. Without such releases, insurers' bad-faith exposure may prevent them from contributing the policies' full limits to settlement. This can be the case even where it would be objectively reasonable to contribute the policies' full limits to settlement, and/or the insurer would otherwise want to do so.

That is not a typo; bad-faith exposure *prevents* an insurer from paying more money to settle. Irony abounds,[26] but how can this be? The answer is this: other insureds.

The problem arises from states' insurance-coverage laws. As one insurance-coverage treatise states, "When two or more insureds are potentially liable for the same injury and their coverage is subject to a single limit, issues can arise if the claimant demands the limit to settle with fewer than all insureds and refuses to agree to a complete settlement."[27]

For example, in some jurisdictions (*e.g.*, New York and California), an insurer cannot settle for one insured eliminating coverage for the other insurer.[28] As stated in *Smoral*, "It is absolutely no answer for the company to say that it paid the full amount of its policy if in so doing it fully protected one of its insureds and left the other completely exposed."[29] In jurisdictions that have held to the contrary, those decisions may also be limited only to circumstances where liability amongst the insureds is joint and several.[30] What's more, a majority of states have not clarified this issue, thus leaving substantial risks for insurers that exhaust limits for only one insured.[31]

With this law, an insurer's "good faith and fair dealing" obligations may compel it to only settle when all insureds are released. This is especially true with mass torts, where different policy limits (aggregate, "per claimant" and/or "per occurrence") might be exhausted. Thus, there is a necessity for third-party, nonconsensual third-party releases. Insurers need to be able to secure releases for parties other than the nondebtor. Without the ability to obtain these releases, settlements become far less likely.

Conclusion

As many courts and commentators have explained, bankruptcy is one of the — if not *the* — best and most efficient defense strategies to ascertain, assess and resolve mass tort liabilities. Nonconsensual, third-party releases are key to that process.

Insurance is often the most vital asset in mass tort bankruptcies, and also likely covers additional insureds with exposure for the same underlying issues. Without such releases, insurers will be less likely to contribute maximum amounts toward settlement for two primary reasons:

1. Insurers will not obtain finality. They still will face future liability from the other insured entities/people.
2. Insurers' good-faith obligations may prevent them from adequately contributing to settlement, and those duties may prevent them from exhausting policy limits without securing releases for the additional insureds.

Without nonconsensual, third-party releases, there is likely to be much less money available for settlement. This means less chance of settlement. The result is that we lose perhaps the best tool available to resolve mass torts: bankruptcy. abi

26 This is particularly true when considering that insurers are also often subject to bad-faith exposure for not making reasonable settlements. *See generally Restatement of the Law of Liability Insurance* 24, cmts. a-d.

27 1 *New Appleman Insurance Bad Faith Litigation* § 2.03[9][b].

28 *Strauss v. Farmers Ins. Exch.*, 31 Cal. Rptr. 2d 811, (Cal. Ct. App. 1994); *Smoral v. Hanover Ins. Co.*, 322 N.Y.S.2d 12, 14 (N.Y. App. Div. 1971). *See also Contreras v. U.S. Sec. Ins. Co.*, 927 So. 2d 16, 22 (Fla. Dist. Ct. App. 2006) (concurring). A few states have intermediate positions where the insurer must first attempt to include all insureds in the settlement before settling for less than all the insureds. *Contreras*, 927 So. 2d at 21-22. "The Alaska Supreme Court has taken an intermediate position, holding that the insurer should seek the release of all insureds and, if unable to obtain that, should file a declaratory action to determine its obligations." 1 *New Appleman Insurance Bad Faith Litigation* § 2.03[9][b].

29 *Smoral*, 322 N.Y.S.2d at 14.

30 1 *New Appleman Insurance Bad Faith Litigation* § 2.03[9][b].

31 *Id.*